



Texas Department of Insurance

333 Guadalupe Street P.O. Box 149104 Austin, Texas 78714-9104
512/463-6169

February 2, 1998

ATTN: Opinions Committee
The Honorable Dan Morales
Attorney General of Texas
P.O. Box 12548
Austin, Texas 78711-2548

RO-1079

FILE # ML-40023-98 Opinion Committee

I.D. # 40023

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Re: Request for opinion regarding the reasonable costs necessary to refinance existing debt secured by homestead property.

Dear Attorney General Morales:

Pursuant to section 402.42 of the Texas Government Code, the Texas Department of Insurance (TDI) seeks the opinion of the Attorney General regarding what constitutes reasonable costs necessary to refinance a debt for purposes of Section 50(e) of the newly amended Section 50, Article XVI, Texas Constitution, as adopted by Texas voters November 4, 1997 (the "Amendment," herein).

The Amendment greatly expands the kinds of loans that may be secured by homestead property. At the same time, the Amendment contains many restrictions. Section 50(e) of the Amendment provides that a refinance of debt secured by a homestead that includes the advance of additional funds may not be secured by a valid lien against the homestead unless the advance of all additional funds is for reasonable costs necessary to refinance the debt. Yet, the Amendment does not define what is reasonable or necessary. If a court later determines that the additional funds advanced were not reasonable and necessary, the loan and lien will be invalid.

The Mortgagee Policy of Title Insurance promulgated by TDI, contains several Exclusions From Coverage, which cannot be modified by the parties. Item 5 of those exclusions precludes coverage due to the invalidity or unenforceability of the lien of the insured mortgage due to any consumer credit protection or truth in lending law. Specifically, this exclusion states,

The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorneys' fees or expenses that arise by reason of...[i]nvalidity or unenforceability of the lien of the insured mortgage, or claim thereof, which arises out of the transaction evidenced by the insured mortgage and is based upon usury or any consumer credit protection or truth in lending law.

Any claim resulting from a court decision declaring the advanced closing costs on a refinance loan secured by homestead property to be unreasonable or unnecessary might be denied under the exclusion for violations of consumer credit protection laws.

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Lenders are asking title companies whether various percentages of the original loan will qualify as reasonable and necessary costs for a refinance loan under the home equity amendment. Yet any such representations by title companies may suggest to lenders that the company is waiving the consumer protection exclusion in Item 5 of the Exclusions From Coverage.

TDI therefore requests the Attorney General's opinion regarding what are "reasonable costs necessary to refinance such debt" for purposes of Section 50(e) of the Amendment? Enclosed is a copy of recent correspondence from Chicago Title Insurance Company, dated January 22, 1998, and TDI's initial response, dated January 28, 1998.

Thank you for your attention to this matter. If you need additional information, please contact TDI's Deputy Commissioner for the Title Insurance Division, Robert Carter, at 305-7402.

Sincerely,



Mary Keller
Senior Associate Commissioner
Legal & Compliance Division

Enclosures

CHICAGO TITLE INSURANCE COMPANY

7616 LBJ FREEWAY, SUITE 300, DALLAS, TEXAS 75251
P.O. BOX 740248, DALLAS, TEXAS 75374-0248 (972) 934-0077



AGENCY DEPARTMENT
DALLAS OFFICE

January 22, 1998

The Honorable Elton Bomer
Commissioner of Insurance
Texas Department of Insurance
333 Guadalupe
P.O. Box 149104
Austin, TX 78714-9104



Dear Commissioner Bomer:

A major issue has arisen in the title insurance industry involving the recent Constitutional Amendment permitting equity lending secured by homesteads in Texas. Specifically, a refinance lien may be held void if the costs of the loan rolled into the total loan transaction are determined to be *unreasonable or unnecessary*. If a refinance lien insured by a Texas Form Mortgagee Policy is later held to be void because the costs of the loan rolled into the total loan amount are deemed to be unreasonable and/or unnecessary, and if the refinance lien is held to be subject to Consumer Protection Laws, the title insurance underwriter would be compelled to deny coverage to the lender pursuant to paragraph 5 of the Exclusions From Coverage of the Texas Form Mortgagee Policy.

There is no definition in the statute or in case law for what is *reasonable or necessary*. Therefore, in the absence of a definition for reasonable and necessary, a title insurance underwriter has no basis upon which to offer coverage beyond the four corners of the currently promulgated forms of insurance.

There is obvious confusion within our industry regarding this issue which has given rise to certain lenders that believe they can secure coverage from those title insurance underwriters that are willing to represent that a certain percentage of loan costs may be rolled into the refinance lien, and are suggesting they will not assert the Consumer Protection Exclusion as a defense. In effect, lenders relying upon this misunderstanding are "blackballing" any title insurance underwriter that will not provide coverage up to a certain percentage amount.

I appeal to your review of this matter at your earliest possible opportunity. Because of the severe penalties being placed upon my companies and other companies in our industry, a directive from your Department is imperative.

Specifically, we believe that the Texas Department of Insurance should immediately notify the title insurance industry that under no circumstances should coverage be offered or implied to any lender *if* the refinance lien is later held to be void and *if* the lien is subject to a Consumer Protection Law. Furthermore, it should be made clear to the title insurance industry that the

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T. GRIFFIN
G. SLOTT
H. H. HUGHES

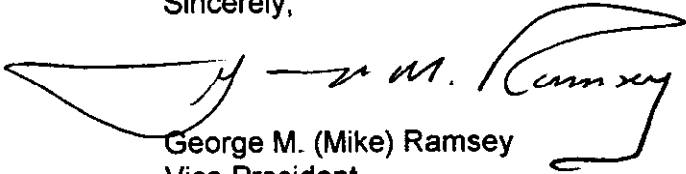
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lender is ultimately responsible in the event a lien is found to be invalid and was otherwise subject to any Consumer Protection Law.

Thank you for your assistance in this matter and I again respectfully urge your immediate action due to the significant impact this issue bears on the title insurance industry.

Sincerely,

A handwritten signature in black ink, appearing to read "George M. Ramsey", is written over a horizontal line. The signature is stylized with a large, sweeping initial "G" and a long, horizontal stroke extending to the right.

George M. (Mike) Ramsey
Vice President
Central Division Agency Manager

GMR/djd

cc: Robert R. Carter, Jr.
Deputy Commissioner of Title Division

Texas Department of Insurance

333 Guadalupe Street P.O. Box 149101 Austin, Texas 78714-9101
512/463-6169

January 27, 1998

Mr. George M. Ramsey
Vice President – Central Division Agency Manager
Chicago Title Insurance Company
7616 LBJ Freeway, Suite 300
Dallas, TX 75251

Dear Mr. Ramsey:

Thank you for your letter of January 22, 1998 regarding the recent Constitutional Amendment permitting equity lending secured by homesteads in Texas. You are correct that the Amendment provides that a refinance lien may be held void if the costs of the loan are determined to be unreasonable or unnecessary. Yet, the Amendment does not define what is reasonable or necessary.

While this agency lacks authority to define these constitutional terms, I note that the Amendment itself establishes a three per cent (3%) cap for origination expenses for a home equity loan. Texas Constitution art. 16, §50 (a)(6)(E). This indicates that three per cent (3%) might be a safe harbor for bona fide expenses connected with a refinance loan. Texas Constitution art. 16, §50 (s). On January 6, 1998, a Regulatory Commentary on Equity Lending Procedures was issued jointly by the Office of Consumer Credit Commissioner, the Department of Banking, the Savings and Loan Department, and the Credit Union Department. A copy of that Regulatory Commentary is enclosed for your convenience. Section 6(E) of the Regulatory Commentary provides additional interpretive guidance for the calculation of the three per cent (3%) cap as regards home equity loans. Nevertheless, lenders, borrowers, title agents, and title underwriters should beware that the definition of what are reasonable or necessary expenses for a refinance loan will ultimately be for the courts to decide, and may well vary on a case by case basis. Various state and federal consumer protection laws should also be consulted.

I have instructed my Title Division to prepare a bulletin for immediate distribution to all title agents and underwriters warning against the practices described in your letter. Specifically, the bulletin will caution agents and underwriters against suggesting in any way that the Consumer Protection Exclusion in Schedule B of the standard Mortgagee's Policy can be waived or that coverage can be promised for anything outside the promulgated form. Under no circumstances should coverage be promised, offered, or implied to any lender as protection

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Y29 faxed to George Ramsey
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Mr. George M. Ramsey
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against a refinance lien later being held void because it runs afoul of a consumer protection law.

Additionally, I will schedule a rule making hearing to consider whether the promulgated form for the standard Mortgagee's policy should be amended to clarify the impact of the Constitutional Amendment on Schedule B. Finally, I will seek a legal opinion from the Attorney General's Office regarding the definition of what is a reasonable and necessary expense for a refinance loan.

Thank you for contacting my office about this issue. Should you need additional assistance or information feel free to contact my Deputy Commissioner for Title, Robert Carter, at (512) 305-7402.

Sincerely,

A handwritten signature in black ink, appearing to read 'Elton Bomer', with a long horizontal flourish extending to the right.

Elton Bomer
Commissioner of Insurance

EB/rc
Encl

cc: The Honorable J.E. "Buster" Brown